Docket No: 07-0271/
07-0242 Consol.
Bench Date: 3/26/08
Deadline: N/A

M E M O R A N D U M

TO: The Commission

FROM: Eve Moran and David Gilbert, Administrative Law Judges

DATE: March 20, 2008

SUBJECT: North Shore Gas Company
The Peoples Gas Light and Coke Company

Proposed general increase in natural gas rates. (tariffs filed March 9, 2007)

RECOMMENDATION: Deny Rehearing except for Hub Revenue Sharing
Deny AG's Motion for Stay

The Illinois Commerce Commission entered a final Order in this rate case on February 5, 2008. It was served on February 7, 2008.

Thereafter, individual Applications for Rehearing were filed by:

North Shore Gas Company and Peoples Gas, Light and Coke Company ("the Utilities") on March 6, 2008; Illinois Industrial Energy Consumers ("IIEC") and the University of Illinois on March 7, 2008; Multiut Corporation on March 7, 2008; People of the State of Illinois ("AG") on March 10, 2008. The City of Chicago and the Citizens Utility Board ("City/CUB") also filed a joint application on March 10, 2008.

Section 10-113 of the Illinois Public Utilities Act states, in relevant part, that:

> Within 30 days after the service of any rule or regulation, order or decision of the Commission any party to the action or proceeding may apply for a rehearing in respect to any matter determined in said action or proceeding and specified in the application for rehearing. 220 ILCS 5/10-113.

The law further holds that the Commission shall receive and consider such application and shall grant or deny such application in whole or in part within 20 days from the date of the receipt thereof by the Commission. *Id.* Here, each of the Applications was timely

filed and, pursuant to law, the Commission must take action on the pleadings no later than March 26, 2008.

In this second half of their memorandum, the Administrative Law Judges ("ALJs") are addressing all the remaining contentions raised in the applications for rehearing.

I. RATE BASE

A. Gas in Storage – Working Capital

(Utilities' Rehear. App. at 11)

The Utilities observe the Order to have approved Staff's proposed adjustment to Gas in Storage for "working capital." Order at 27. They contend that this decision is not supported by substantial evidence, is against the manifest weight of the evidence, for the reasons established in the evidentiary record as shown and referenced in the Utilities' briefing. According to the Utilities, the evidence shows that the disallowed costs were prudently incurred and reasonable in amount, and, therefore, should be included in rate base either as working gas or as base gas. As such, they ask the Commission to grant rehearing and, based on the evidence in the record, to not adopt Staff's proposed adjustment and thus revise the Order in that respect.

The Commission needs to be shown with some specificity where and how it has erred. The Utilities have not, in this instance, made such a demonstration. Thus, no grant of rehearing is warranted or recommended.

B. OPEB Liabilities, Pension Asset/Liability, and Pension Contributions

(Utilities' Rehear App. at 11-12)

The Utilities contend that the Order (at 36) erroneously approves Staff's proposed adjustments to OPEB liabilities without making any modifications to incorporate the Utilities respective pension asset/liability or their test year pension contributions. This decision, they argue, is not supported by substantial evidence and is against the manifest weight of the evidence, for the reasons set out in the evidentiary record as shown and referenced in the Utilities' briefing. The Utilities claim too, that Staff's (and GCI's similar) proposed reductions are incomplete and one-sided. According to the Utilities, the OPEB liabilities reductions should not be adopted, or in the alternative if the OPEB liabilities are to be deducted, then Peoples Gas' test year contributions of $15,278,614 and North Shore's test year contributions of $1,862,247 to the pension plan should be incorporated in the calculation of their rate bases. They ask the Commission to grant rehearing and, based on the evidence in the record, reconsider its decision and so revise the Order; or, in alternative, approve the proposed adjustments subject to the pension contribution offsets.

The Utilities' application for rehearing fails because it is insufficiently detailed. It does not point to any error in reasoning or analysis. As such, no rehearing is warranted.

C. Reserve for Accumulated Depreciation and Amortization

(AG Rehear. App. at 44-49) (City/CUB Rehear. App. at 5-18)

Both the AG and City/CUB ask that the Commission reconsider its Order and approve the *pro forma* rate base adjustment to recognize changes in accumulated depreciation, as proposed by GCI witness David Effron. The arguments set out by these parties, however, are no clearer, sounder or more persuasive on rehearing, than when presented on briefs.

In large part, the AG and City/CUB complain that the decision in this case follows in line with the conclusion set out by the Commission in an earlier order. The no *res judicata* notion only means that the Commission can react to new and different evidence. On balance, however, the Commission must also keep in mind that it cannot act an arbitrarily or capriciously such that it will be called upon to distinguish and explain differences in treatment. In the end, the GCI parties offer nothing meaningful to support a claim of error. Notably, and still today, they are unable to give support or explain why the Commission should treat like situations differently. Thus, there is no reason to grant rehearing.

II. OPERATING EXPENSES

A. Incentive Compensation Expenses

(Utilities Rehear. App. at 12-14)

According to the Utilities, the Order (at 66) errs, as a matter of law, is not supported by substantial evidence, and is contrary to the manifest weight of the evidence, because it denies recovery of the full amounts accrued under the "TIA" plan, as well as denying recovery for certain costs and expenses under certain other incentive compensation plans.

The Utilities urge the Commission to grant rehearing and, based on the existing evidentiary record, to approve all of the incentive compensation program costs and expenses that were included in the Utilities' proposed revenue requirements (except that Utilities do not seek rehearing as to the Short-Term Incentive Compensation ("STIC") plan costs and expenses). They maintain that briefing on this issue shows that the costs and expenses associated with these programs benefit the Utilities' customers through attracting and retaining a sufficient, qualified, and motivated work force, as well as other customer benefits. The Utilities claim they are entitled to recover costs and expenses that were reasonable and prudently incurred. And, they assert, these programs satisfy the Commission's additional requirement that incentive compensation not only be prudent and reasonable in amount, but also benefit a utility's customers.

Utilities contend that the 2006 "TIA" plan applied to non-officer, non-union employees and encompassed both financial and operational performance measures, and complete recovery of the $1,642,847 paid out ($1,502,485 by Peoples Gas and $140,253 by North Shore) is appropriate. With respect to Affiliate Charges, the Utilities should be allowed to recover $744,812 charged to Peoples Gas and $165,811 charged to North Shore (or, at a minimum, 37.5% of these charges, which represents costs associated with the operational measures of that program). Finally, the Utilities assert they should be allowed to recover $1,756,000 for costs associated with Restricted Stock and Performance Shares programs. The Restricted Stock program was based on providing a competitive compensation package, not "financial" measures, although the Performance Shares program was based on "financial" measures. Alternatively, as to those last two programs, at a minimum, the Utilities argue that they should be allowed to recover $1,529,000 for the non-financial measures under the Restricted Stock program.

The Utilities claim to have met their legal burden on the issue of recovery of incentive compensation by demonstrating that the Plans are prudent, reasonable in amounts, and, are necessary and useful to attract and retain sufficient, quality workers, as well as resulting in other tangible benefits to ratepayers, such as controlling O&M expenses and increasing customer satisfaction. Accordingly, the Utilities seek rehearing and recovery of the full amount of incentive compensation costs and expenses included by the Utilities in their proposed revenue requirements, except, again, the Utilities do not seek rehearing as to the STIC plan costs and expenses.

The Utilities repeat essentially the same arguments made at the briefing stages. This does not suffice on an application for rehearing. It is essential to identify what evidence the Order overlooked, what fact it wrongfully exalted or what law it misconstrued. The application at hand does not show, with any clarity, that the Order fails in reasoning or analysis.

Thus, rehearing is not recommended.

III. HUB SERVICES – REVENUE SHARING

(IIEC Rehear. App. at 7-9)

The IIEC and other parties asked, on brief, that HUB revenues be credited to both sales customers and PGA customers. Staff, however, had concerns. Given the timing and manner of this proposal, Staff had no opportunity to offer testimony on the matter.

The Order reflected a need to hear from all interested parties on the matter and thus rejected the IIEC proposal. While there is not sufficient record evidence for the Commission to rule differently at this point, the ALJs believe that the matter should be fully and fairly litigated. In other words, the IIEC's arguments for rehearing grounded on the actions taken in the Nicor rate case, give reason enough for the Commission to consider the question of the sharing of HUB revenues in this case.

Thus, it is recommended that rehearing on this issue be granted.

IV. RIDER VBA

The only parties to challenge the Order's decision on Rider VBA are the AG and City/CUB. Their respective allegations and arguments, however, miss the point. Instead of treating the Order's conclusion as the work of integrated analysis that it is, these parties attempt to fashion a showing of error by picking apart a few select phrases that are taken out of context. At the same time too, they omit and avoid anything in the Order that is not beneficial to their own ends. None of this is useful to the Commission's consideration of a rehearing application.

As the following discussion shows, both individually and cumulatively, the claims of error set out in the applications lack merit.

A. Discretionary Authority

(City/CUB Rehear. App. at 49) (AG Rehear. App. at 22-27)

It is not clear as to what error is being pressed with this line of arguments that do not directly challenge the Order.

At one point, City/CUB maintain that the Commission's approval of Rider VBA is outside its jurisdiction. City/CUB Rehear. App. 50. At another juncture however, these parties flatly acknowledge at the Commission has authority to approve riders. Id. at 27. In any event, there is no meaningful assessment of the difference.

According to the AG, the Order relies on City I as the basis of its "unlimited authority" to approve Rider VBA. AG Rehear. App. at 23. The AG is confused on many counts. First, City I is but one of many opinions that the Commission studied and relied on in the situation. Second, the Order does not state nor does it imply that the Commission has unlimited authority to adopt Rider VBA, or any other rider. To the contrary the Order recognizes that the Commission has discretionary authority and that is a much different thing.

And, it is evident that the Commission does not take its discretionary authority lightly. Indeed, the Order derives, after lengthy and careful case law review, that:

> We accept our discretionary authority to approve the rider mechanism in any given situation must rest, not simply on our inclination, but on the basis of our sound and reasoned judgment. Order at 150.

Notably, none of the applications can, or do, take issue with this pronouncement.

On the argument presented, rehearing is not warranted.

B. Single-Issue Ratemaking.

(City/CUB Rehear. App. at 27-36) (AG Rehear. App. at 8-)

The City/CUB draw attention to the Order's discussion of BPI where the Court wrote of the formula designed to determine the revenue requirement and where it observed that it would be improper to consider changes to components of the revenue requirement in isolation while tending to this process. The City/CUB make no claim that the Order is wrong in referring to this opinion or in relying on the other case law. These parties simply assert that the BPI Court's opinion favors their position that Rider VBA is unlawful. But, they cannot effectively or correctly draw this conclusion in a rider situation without considering all of the case law authority discussed in the Order. This, however, these parties do not do.

The AG attempts to suggest that the opinions in CUB, City, and Archer-Daniels should not be considered in terms of the legal principles these courts establish, but only as to the particular facts situations in those cases. As such, and in the AG's view, Rider VBA is not like the costs or expenses at issue in any of these cases.

The problem with the AG's arguments is that, in construing arguments on single-issue rulemaking in the rider situation, the courts have never limited the principles they set out to any particular fact pattern. Indeed, the only time that a court's opinion was considered to be fact-limited was with respect to Finkl. See Order at 144. Thus, the AG wrongfully attempts to create a standard that the courts themselves did not deem proper to impose.

Where there is no error demonstrated in the Order's full and complete analysis of the issue, no rehearing need be granted.

C. Retroactive Ratemaking

(City/CUB Rehear. App. at 37-41) (AG Rehear. App. at 12-15)

The City/CUB contend that the Order's conclusion on retroactive ratemaking is based on a misunderstanding of case law. City/CUB Rehear. App. at 38. These parties, however, never discuss the case law authority on which the Order relies, much less offer up any different interpretations of same.

Nothing in the AG's application reflects an understanding of the rule. Rider VBA does not, as the AG claims, come into being after rates have been established. It is part and parcel of the rate setting. Even more egregiously, the AG skirts around and ignores the most critical parts of the Order's analysis.

Referring to the symmetrical operation of Rider VBA, the AG claims that these are the kinds of retroactive adjustments that "Illinois courts have held to be illegal." AG Rehear. App. at 13. Notably, however, the AG provides *no* authority for this assertion. As such, the argument has no merit.

On all the arguments presented, the AG's application must fail. Likewise, the application of City/CUB must also fail. Rehearing is not recommended.

D. Test Year Rule

(City/CUB Rehear. App. at 41-42) (AG Rehear. App. at 15-18)

City/CUB take issue with the Order's conclusion that Rider VBA does not violate the test year rule because "the base rates that are approved in this case and which are the basis for the margin revenues to be recovered under Rider VBA have been evaluated in accordance with the appropriate test year prescriptions." City/CUB Rehear. App. at 41.

But, they do not explain how or why this statement is in error. Most notably, they ignore the pronouncements and sound analysis of the test year rule that was set out by the Illinois Supreme Court in CUB v. ICC. It is this authority upon which the Order relies. See Order at 146.

The AG is right in asserting that the instant proceeding involves a general rate case. But, it fails to understand what this means in terms of the test year rules as established by the Illinois Supreme Court in CUB v. ICC. The Order follows in line with the relevant case law and, despite all the doubts that the AG attempts to raise, the Commission's reliance on this authority is not shown to be erroneous.

In short, the Order's conclusion of no test year violation with respect to Rider VBA is not demonstrated to be wrong. Therefore, rehearing is not recommended.

E. Incentive Regulation

(City/CUB Rehear. App. at 42-44)

The City/CUB assert that promoting energy efficiency is good policy. As such, they maintain that the Commission "could have conditioned its approval of Rider VBA on Peoples Gas' and North Shore's argument to invest additional money in energy efficiency programs." City/CUB Rehear. App. at 43. And, they even ask that the Commission do so on the granting of their requested reconsideration of the Order. These arguments come too late and are in disregard of the evidence.

The City/CUB fail to understand that the Commission must and did consider the entirety of the record in the making of its decision. The whole of the record shows that the Utilities did propose energy efficiency programs in this proceeding. And, no party ever contended that the amount proposed for the programs was insufficient. City/CUB also fail to understand that the Commission itself was never bound to that proposal. It was always free to reject it. But, if the Commission were to consider the Energy Efficiency Programs to be appropriate, then it also had to consider what consequences would likely bear on both utilities and its customers as a result of this effort. This it did.

In an odd juxtaposition, City/CUB further suggest that Rider VBA amounts to incentive-based regulation as governed by Section 9-244 of the PUA and requires that a formal petition be brought under that provision. Insofar as City/CUB would claim error on grounds that a Section 9-244 petition was required in these premises, they demonstrate nothing on the point. In the ALJs' view, this argument is a red herring.

In the final analysis, these parties do not directly address the Order's understanding, discussion or conclusion in the matter. Thus, rehearing is not recommended.

F. Discrimination

(City/CUB Rehear. App. at 44) (AG Rehear. App. at 27-30)

The City/CUB claim that Rider VBA violates the prohibition against "unreasonable" rate discrimination. This, they summarily argue, comes from the Order's reduction of each utility's return on equity by 10 basis points, which operates to benefit all class rates. Underlying this argument is the theory that the cost of capital varies by customer class. Such a concept, however, has never been embraced by the Commission. Thus, this claim has no merit.

The AG claims that there is no evidence to show that weather variability, use per customer and conservation measures are unique to residential and small customers. The AG explains, however, that the Intervenors who worked with the Utilities in constructing the parameters of the Energy Efficiency Program "purposely" omitted large users from the program because they were already making investments in energy efficiency.

So too there were other differences to be analyzed and explored, e.g. different usage patterns between large and small users, or differences in their respective monthly charges, if unreasonable discrimination was a concern. But, this is not of record and has not been proven. That is what the Order concludes and it has not been shown to be wrong. Thus, rehearing is not recommended.

G. Revenues

(City/CUB Rehear. App. at 45-46) (AG Rehear. App. at 27-30)

The City/CUB contend that the opinion in Finkl reviewed the only rider that provided, in part, for the recovery of lost revenues. And, they observe that this feature was among the many grounds upon which the Finkl court rejected the rider. They also correctly note that the Order sets out several differences between Rider VBA and the rider at issue in Finkl. But, as to their claim of error, the City/CUB contend that the Commission cannot ignore Finkl and that all of the distinctions set out in the Order are not persuasive.

It is true that the Finkl opinion stands. But it is also true that many aspects of Finkl have been distinguished and explained away in subsequent court opinions. What is abundantly clear from Finkl, and what the Order reasonably derives, is that the Finkl court did not perform a true rider analysis owing to its determination that a rate case was required in the premises. This wash colours nearly everything that the Finkl court wrote. Both the underlying conditions and the rider at issue here are much different than in Finkl and, as subsequent case law shows, require a different analysis.

The AG claims that the Order's reading of Finkl is wrong and should be revisited. But nothing that it points to, or argues, is persuasive.

With there being no error shown, no rehearing is recommended.

H. Substantial Evidence

(City/CUB Rehear. App. at 46-48) (AG Rehear. App. at 32-37)

> Substantial evidence is defined as evidence which a reasoning mind would accept as sufficient to support a particular conclusion and consists of more than a mere scintilla of evidence but may be somewhat less than a preponderance. **Abbott Laboratories v. ICC**, 289 Ill. App.3d 705 (1st Dist. 1997).

The City/CUB contend that there is no substantial evidence to support the Order's concern about variable customer usage and the resulting impact on the utilities' revenues. At the same time, however, City/CUB themselves point out that customer usage has been declining, and by almost a third, since the Utilities' last rate case. This evidence notwithstanding, the City/CUB claim there is no need for concern because the utility earned their authority return in "most years" since. To press this argument, these parties ignore the more recent revenue shortfalls evidenced on record, illustrated in the Utilities' briefs, and presented to the Commission in oral arguments.

Further, the City/CUB observe that the Order supports its decision under its policy to promote additional investment in energy efficiency programs. According to City/CUB, they "wholly" embrace this policy. But, they also express concern that the utility has no plans to "increase EEP" if Rider VBA is approved. What these parties apparently believe is that Rider VBA is not problematic if it can be tied to higher EEP spending. The record is such, however, that no greater amount of spending on EEP was proposed by City/CUB or the AG, not even as an alternative measure.

In making their respective arguments, the AG and City/CUB do not consider what is of record:

- The facts of this case show that gas usage is declining and that the Utilities' high fixed costs are not declining.

- The facts of this case show that energy efficiency is a much needed resource and that the Utilities are proposing, against tradition and interest, an energy efficiency program.

- The facts of this case show that energy efficiency, weather variability, and conservation are realities and affect the Utilities' fixed cost recovery.

- The facts of this case show that other means for recovery of fixed costs are employable, but neither the AG nor City/CUB has advocated for such a rate design.

It is this record evidence, in part, that the Order considered. It is also this evidence that undermines the AG and City/CUB claim of error. For all the reasons, rehearing is not warranted.

I. Procedural Process

(AG Rehear. App. at 40-44)

The AG's Application for Rehearing has it wrong when challenging the procedural process of this case. This is made abundantly clear by the AG's failure to allege, much less show, any harm or prejudice.

The Proposed Order issued on November 26, 2008 and, in terms of Rider VBA, it passed on the legal issues in the matter. While case law authority had been cited to in the various parties' brief, no meaningful analysis as called for in the situation was offered. Nevertheless, as the Briefs on Exceptions came in, it became obvious that *all* of the parties were urging that the legal issues be addressed.

ALJ Moran told the Commission of this development at the Opening Meeting on January 16, 2008, and indicated that she would indeed be responding to these exceptions with a complete and thorough legal analysis. This statement was made at the time when the ALJs were providing the Commission with highlights and observations on all of the contested issues discussed in the Proposed Order. Contrary to the AG's assertion, there was no direction given to the ALJs to prepare a new substantially-altered PEPO.

A PEPO is intended to respond to the parties' Briefs on Exceptions and Replies to Exceptions. It gives the Commission (through the ALJ) an opportunity to clarify, amend or modify its decisions. Indeed, a party is required, under the Commission's rules of practice, to not only argue why any portion of the Proposed Order is incorrect, but also to provide alternative recommended language in the event that the Commission is persuaded. This is standard and long-standing practice.

The AG is correct to note that at the Open Meeting on January 16, 2008, ALJ Moran made known in that public forum that the recommended conclusion of Rider VBA had changed. (And, as it turned out, there was much added, rewritten or changed in the

PEPO on other issues). The AG correctly notes the ALJs' Memo of January 8, 2008, to state, in part, that:

> In rejecting Rider VBA, the ALJPO (the November 26 Proposed Order) meant to foster discussions among the parties and a better understanding of Rider VBA through meetings or workshops. This did not happen. And in their exceptions argument, the GCI point out that the presence or absence of consensus is irrelevant to the Commission's conclusion on the law and evidence. Further, these parties maintain that no consensus was possible because Rider VBA is illegal and the evidence did not support it.
>
> The PEPO finds differently and on both counts. It does a full and comprehensive legal study (as called for in the circumstances) and concluded that Rider VBA is lawful.

The AG's Application fails to provide a complete picture. Where a detailed legal analysis appeared in the PEPO, and proved itself contrary to the summary arguments of all parties, ALJ Moran recommended that the PEPO be distributed to the parties so that they could well prepare for oral argument. The Commission agreed.

Oral argument on a number of issues, including Rider VBA was held on January 23, 2008. The AG, having been served a copy of the PEPO did present arguments on Rider VBA. As such, the AG was not prejudiced and particularly so because the case law authority analyzed for the PEPO was the same case law that was identified in the parties' and the Staff's initial briefs.

To be sure, the AG filed a motion asking for release of the PEPO and leave to file another round of briefs. The ALJs considered the request and denied same for reason that:

> The Motion filed by the Attorney General on January 16, 2008 is summarily denied. The Commission has already decided to release the PEPO to the service list for purposes of oral argument and thus, the AG's request in this regard is moot.

With respect to the AG's further request of having the parties be permitted to file briefs or comments in response to any new conclusions or other substantive changes as set out in the PEPO, the ALJs consider it clear that changes in the PEPO were contemplated by the arguments of the parties when filing both their respective exceptions and replies to exceptions. There is no right to an additional round of written argument when in fact such change occurs in due course. Moreover, the Commission exercised its discretion to allow both oral argument and the extraordinary release of the PEPO prior to the entry of a final order.

Notably, the AG did not seek Commission review of this ALJ ruling. Yet, the AG had both the right and the opportunity to do so. So too, in this application, the AG does not point to any new law or case authority or any new facts that it was unable to present

to the Commission through another briefing. In other words, without such a showing, no harm or prejudice can be presumed.

At another point, the AG faults the Proposed Order for being inadequate under the law. Even if true, however, the AG, like any other party has a remedy. It can point out all the shortcomings, errors, etc. in a brief on exceptions to that Proposed Order. The AG did so here and filed a multitude of pages of arguments on Rider VBA alone.

The AG seems to specifically fault the Proposed Order for stepping aside and attempting to have the parties reach a consensus on Rider VBA. Yet, it is the AG which continuously and strenuously argued that, in other jurisdictions, the adoptions of decoupling mechanisms, like Rider VBA, were achieved in the course of settlements. Perhaps the timing was not ideal for this activity but the ALJs still considered it doable and, given the AG's arguments, desirable.

Assuming arguendo that the AG still had new laws, facts or arguments bearing on the issue of Rider VBA, it is given the instant opportunity. The law gives the AG, and all parties, 30 days to prepare an Application for Rehearing. This is yet another means for bringing to the Commission the reasons why it should reconsider its Order. But, the contentions presented must be meaningful.

In the final analysis, the AG has been provided abundant process for making its case. On the whole, and in the particulars of what it has alleged, the AG has demonstrated no harm or prejudice. As such, rehearing is not warranted and not recommended.

J. Modifications to Rider VBA

(City/CUB Rehear. App. at 48) (AG Rehear. App. at 39)

The City/CUB assert that the Order's decision to implement Rider VBA as a four-year pilot program is a good consumer safeguard. City/CUB Rehear. App. at 48. Further, the City/CUB take note that the Order directs Staff to file annual reports with respect to the impact of Rider VBA on the Utilities' rates of return. But, these parties appear to want something more of an explanation for these safeguards and some criteria for assessment. Among other things, the AG takes issue with the Order's direction which requires Staff to provide "annual Reports" on the Utilities' rate of return and Rider VBA's effect on that return. This is a hollow safeguard, the AG asserts, because Staff is given no direction on how to make its evaluation.

There is nothing meaningful or correct in these contentions. The Commission Staff has extensive expertise and experience in reviewing records and reports on all types of regulatory matters. The Commission has no reservations in entrusting to its Staff the task at hand. Based on past experience, Staff will not hesitate to ask for any clarification it might need. Moreover, the parties overlook other protections set out in the Order

Given full opportunity to present any other options or any new or revised safeguards, the applications are bare. It is not enough to say that what the Commission has done may not be to our liking. It is essential to set out clear and solid proposals. The AG had every opportunity to propose safeguards in the event that Rider VBA was adopted. There is nothing on record. If City/Cub had a set of criteria, it should have proposed same in this proceeding or at the very least, in their application. In the end, there is nothing for the Commission to consider.

In essence, the applications do not show that any of these parties have anything to bring to the table on rehearing. Thus, it would be an empty exercise. Rehearing is not recommended.

K. Further Legal Arguments

(AG Rehear. App. at 3-8; 30-32)

The AG contends that the basic concepts in the landmark case Bluefield Waterworks Improvement Co. v. Public Service Comm'n of West Virginia, 262 U.S. 679, 692-693 (1923), the U.S. Supreme Court established that a utility's rates should reflect the opportunity – not a guarantee – to earn a return on its used and useful property when a commission sets rates. So too, the Supreme Court elaborated on the principles governing rate of return regulation in the case of Federal Power Commission v. Hope Natural Gas Company, 320 U.S. 591 (1941). And, the Supreme Court reaffirmed in Federal Power Commission v. Natural Gas Pipeline Co., 315 U.S.575, 590 (1942) that "regulation does not insure that the business shall produce net revenues." Hope Natural Gas, 320 U.S. at 603.

The AG pulls out phrases from long-standing court opinions and gives no context for these pronouncements. Nor does it account for evolutionary changes brought by time and circumstance. For example, it is of record that decoupling mechanisms have been approved in at least 13 states across the nation. It is inconceivable that this could or would be done in light of the AG's strict arguments. Whereas, the AG made much of the fact that these were the result of settlements, we are not persuaded as to any difference. No regulatory body is able to approve a settlement that is in violation of law.

The AG further asserts that Illinois courts have adopted the Hope and Bluefield standards and applied them to the regulation of utilities in Illinois. In this regard, the AG points out that, "The rate making process under the act, i.e., the fixing of 'just and reasonable' rates[,] involves a balancing of the investor and the consumer interests.' " Illinois Bell Telephone Co. v. Illinois Commerce Comm'n, 414 Ill. 275, 287 (1953) quoting Federal Power Comm'n v. Hope Natural Gas Co.

What is disturbing in this argument is that the Order sets out the very same proposition of law. See Order at 152. Indeed, it is this balancing of interests, here being called for by the AG, that the Order actually employs.

At another point, the AG also refers to the attribute of "least-cost," a term that appears in certain provisions of the PUA. But, the AG performs no statutory analysis of any of the sections where the term appears. This the intent of General Assembly in enacting this legislation and its particular placement in the PUA has never been established. This is critical where the statutes themselves appear to be largely in the nature of prefatory language. Where such analysis has not been provided by the AG to support its assertion, the Order is not in error for considering same.

Because the AG has not shown the Order to have erred, no rehearing is warranted or recommended.

V. EMBEDDED COST OF SERVICE STUDY

A. Coincident Peak Versus Average and Peak Allocation Methods

(Utilities Rehear. App. at 17)

The Commission held that the Utilities should allocate their distribution system investment using an average and peak ("A&P") allocator, rather than a coincident peak ("CP") allocator. Order at 199. According to the Utilities, the Order errs in its conclusion that the Commission has consistently found the A&P allocator to be preferable to the CP allocator. While the Commission has a recent history of using an A&P allocator for gas utilities, it also has a significant history of using other allocators for distribution system investment. Moreover, in recent electric utility cases, the Commission did not adopt an A&P allocator, despite considering issues similar to those for gas utilities. Also, the Utilities contend, there is compelling evidence for allocating distribution system costs based on design day demand. As such, the Commission's decision is not supported by substantial evidence and is against the manifest weight of the evidence. Accordingly, the Commission should grant rehearing and, on the existing evidence in the record, reverse this adjustment.

In their application, the Utilities raise no new arguments. They do not point to any record evidence that was overlooked. Nothing set out in the application warrants rehearing.

B. Allocation of Distribution Plant Account No. 385

(Utilities Rehear. App. at 18)

Peoples Gas takes issue with the Order's conclusion that Account No. 385 costs should be directly assigned to individual customers for the purpose of determining customer-specific charges. Order at 211. According to Peoples Gas, it has the capability of assigning many costs, not just Account No. 385, to individual customers, and its embedded cost of service study reflects this fact. The record and the Order give no consideration to the possible impact of designing customer-specific charges for other costs for which company records would permit such recovery. When one account is singled out for this treatment, Peoples Gas asserts, it is not fair and equitable to the group of customers who are singled out. The Commission's decision is not supported by

substantial evidence and is against the manifest weight of the evidence. Accordingly, Peoples Gas seeks rehearing and, on the existing evidence in the record, asks for reversal of this adjustment.

The arguments for rehearing on this issue are not persuasive. There is nothing new. While Peoples Gas suggests a failure to consider the impact of its decision, it is far from clear as to what this means. Hence, rehearing is not warranted.

VI. CORRECTION OF TYPOGRAPHICAL ERRORS IN THE ORDER

The Utilities point out that Order contains certain text that actually appeared in the Post-Exceptions Proposed Order but not revised to reflect the rulings in the Order. More specifically, they set out the typographical errors that should be corrected. These are:

- The introductory sentences to the rate base tables, and the tables themselves, on pages 37-38 of the Order reflect figures in the Appendices to the PEPO, rather than the Appendices to the Order.

- The introductory sentences to the operating expense tables and the tables themselves on pages 70-72 of the Order reflect figures in the Appendices to the PEPO, rather than the Appendices to the Order.

- The ROR and ROE figures on page 102 reflect the rulings in the PEPO and, therefore, need to be corrected to reflect the rulings and figures on pages 100 and 317 and reflected in the Appendices to the Order.

- Finally, the period should be a comma in the approved Peoples Gas rate base figure on page 317 (Finding 7) of the Order.

The ALJs agree with the Utilities' observations and recommend that these necessary corrections be set out in an Amendment to the Order.

VII. THE AG'S MOTION FOR A PARTIAL STAY OF THE COMMISSION'S ORDER OF FEBRUARY 5, 2008 OR, IN THE ALTERNATIVE, MOTION FOR COLLECTION OF RATES SUBJECT TO REFUND.

A. The Motion

The AG filed, pursuant to Illinois Supreme Court Rule 335(g) and 83 Ill. Admin. Code 200.190, a motion to stay implementation of those portions of the February 5, 2008 Order that authorize the Utilities to collect revenues under tariffs implementing the decoupling rider, Rider VBA.

In the alternative, the AG asks that the Commission enter an order that provides that all revenues collected pursuant to the February 5, 2008 Order be subject to refund pending the outcome of the People's appeal of both that Order, and any Order that may

be issued by the Commission denying the People's Application for Rehearing on the Rider VBA issue.

In support of this Motion, the AG states that:

1. The Order approves Rider VBA, a tariff that assesses monthly surcharges on Rates 1 and 2 (residential and small business) customer bills when usage per customer levels fall below a usage-per-customer benchmark identified in the Order. This tariff is scheduled to go into effect next month.

2. This Rider VBA tariff is both unlawful and unsupported by the record evidence.

3. Supreme Court Rule 335(g) provides that "[a]pplication for a stay of a decision or order of an agency pending direct review in the Appellate Court shall ordinarily be made in the first instance to the agency." Ill. Supreme Court Rule 335(g).

4. If the Commission denies the AG's Application for Rehearing or grants rehearing but fails to reject Rider VBA, the People expect to file an appeal in the Illinois Appellate Court of the Commission's Order and any order denying rehearing.

5. The Court that obtains jurisdiction of the appeal is not likely to rule on the People's appeal for several months. Rider VBA surcharges will begin appearing on customer bills in April of 2008, according to the Companies' tariffs filed in this case. *See,* e.g., PGL Ex. VG-1.1, at 57-60; NS Ex. VG-1.1, at. 55-58.

6. A partial stay of the Commission's Order pending resolution of an appeal is necessary to preserve the status quo during the Commission's rehearing period and during the appellate review of the Commission's Order. Such a stay would prevent irreparable harm to hundreds of thousands of the Utilities' customers who could be required to pay millions more in natural gas delivery charges than required under the status quo ante, with no legal opportunity to be made whole. Under Rider VBA, the AG set out, the warmer the weather, the more likely Peoples Gas and North Shore customers will pay more in delivery service charges. Likewise, the more residential and small business customers reduce their usage of natural gas as a result of conservation, higher natural gas prices, customer-financed insulation measures and appliance purchases, the more likely Peoples Gas and North Shore customers will pay more in delivery service charges under the ratemaking formula in the Rider VBA tariff.

7. The AG states that "good cause" for ordering a stay of an administrative decision is not determined by traditional equitable requirements, but rather requires a showing that an immediate stay is required in order to preserve

the status quo and that the plaintiff has raised at least a fair question as to the likelihood of success on the merits. Markert v. Ryan, 247 Ill.App.3d 915, 917, 617 N.E.2d 1373 (1993). According to the AG, there exists a reasonable likelihood of success on the merits of their appeal (assuming the Commission declines to revisit its decision on Rider VBA in response to the AG's Application for Rehearing), which will raise an important legal issue of first impression -- whether the ICC has the authority to approve a rider that guarantees recovery of a designated revenue per customer level or so-called rate case margin level. Moreover, the appeal would involve a question of statutory interpretation, which the Court reviews *de novo.* Harrisonville Telephone Co. v. Illinois Commerce Comm'n, 212 Ill.2d 237, 247 (2004); Carpetland U.S.A., Inc. v. Illinois Department of Employment Security, 201 Ill.2d 351, 368-369 (2002). The lack of legal support or precedent for Rider VBA at the Commission or under Illinois law raises a "fair question" as to the sustainability of the rider and the success of the appeal.

8. Failure to grant a stay of the Rider VBA portion of the February 5, 2008 Order will cause irreparable harm to hundreds of thousands of Peoples Gas and North Shore Gas residential and small business/commercial customers.

9. A partial stay of the implementation of Rider VBA tariffs does not threaten irreparable harm to the Companies' financial condition. A partial stay of the Commission's Order pending resolution of the appeal is necessary to preserve the status quo during appellate review of the Commission' Order.

10. If the Commission denies the Motion to Stay, the AG requests that rates be collected subject to refund. Unless the Commission grants this alternative request, ratepayers will be irreparably harmed. Once the Commission establishes rates, the Act does not permit refunds if the established rates are too high or surcharges if the rates are too low. Business and Professional People for the Public Interest v. Illinois Commerce Comm'n, 136 Ill.2d 192, 209, 555 N.E.2d 693 (1989) ("BPI I"); Citizens Utilities Co. v. Illinois Commerce Comm'n, 124 Ill.2d 195, 207, 529 N.E.2d 510 (1988). Moreover, if a Commission order that approves a rate increase is subsequently reversed by a court, and the rate increase has not been stayed, the ratepayers are not entitled to any refund for excess charges collected between the effective date of the Commission's order and the date of the court's decision. Independent Voters of Illinois v. Illinois Commerce Comm'n, 117 Ill.2d 90, 510 N.E.2d 850 (1987). In addition, even if a court reverses the Commission's order in part or in whole, the utility can continue to charge the rates originally approved by the Commission until the agency establishes new rates (although the utility is subject to ratepayers' claims for reparations for excessive rates collected from the time of the Court's reversal through the time new rates are approved by the Commission). BPI I, 136 Ill.2d at 242; People ex rel.

Hartigan v. Illinois Commerce Comm'n, 117 Ill.2d 120, 148, 510 N.E.2d 865 (1987). Collecting rates subject to refund protects ratepayers from illegal and excessive rates that cannot otherwise be refunded.

In still other paragraphs, the Motion sets out essentially the same points and arguments in opposition to Rider VBA that the AG presented in its initial round of briefs and in both sets of exceptions briefs. The Order considered these legal arguments and analyzed each one in detail.

B. Analysis

Having considered the rules and all matters plead in the Motion, the ALJs recommend that it be denied on both counts. Moreover, if the Commission agrees, it is recommended that it adopt this analysis as its own, or with modification, and direct the Clerk to incorporate same as part of its Commission action letter to the parties.

Rule 335 provides that an application for a stay of a decision or order of an agency pending direct review shall "ordinarily" be made in the first instance to the agency. Ill. Sup. Ct., R 335 (g). If made to the Appellate Court, or to a judge thereof, the motion shall show that application has been made to the agency and denied, with the reasons, if any, given by it for denial. Id.

1. The standard for a stay, as set out in the AG's motion, is "good cause" and this requires a showing that (1) an immediate stay is required to protect the status quo; and, (2) that the Plaintiff has raised at least a fair question as to the likelihood of success on the merits. The ALJs are unable to make an independent determination on the matter since Rule 335 is silent. But it is reasonable to believe that the AG is correct.

    a. *Status quo* – The Motion does not speak of imminent change to the *status quo.* This pleading is not titled or framed as an emergency motion. According to the AG, the Rider VBA activity that the AG desires to stay first begins in April. As the Commission is rendering a decision on the AG's rehearing application on March 26, the February 5th Order is directly appealable to the Appellate Court. And, a stay may be sought in the Court as Supreme Court Rule 335 (g) provides.

    b. Likelihood of success – based on the AG's application for rehearing, and all the arguments of record, the ALJs are not persuaded that this element is satisfied. Indeed, the legal arguments that are included have all been addressed, and reasonably rejected by the Order. The Order in turn, has analyzed and relied on relevant case law (that the AG has not been able to

distinguish or explain away in the application for rehearing. This speaks volumes on the matter.

2. This Commission is left unclear as to the legal basis for the alternative proposal. Most prominently, the AG has failed to explain the legal underpinnings of such action. Nor has the AG provided a draft order.

For all the reasons, the Motion is denied.

EM/DG:jt